

NCUA News

Senate Committee Passes Credit Union Bill

The Senate Banking Committee adopted legislation April 30 that would allow credit unions to add groups of up to 3,000 to their fields of membership, despite lobbying by bankers to cut the number to 500.

Adopted by a vote of 16-2, the bill now awaits full Senate approval. Similar to H.R. 1151, the Senate bill includes -

- Community Reinvestment Act-like provisions requiring NCUA to examine service to people of modest means within a credit union's field of membership;
- GAAP requirements for credit unions \$10 million and larger; and
- National Credit Union Share Insurance Fund (NCUSIF) equity level and premium changes.

Senator Phil Gramm (R-TX) proposed and later withdrew an amendment to remove the CRA provisions. He promised to offer the amendment again when the bill reaches the Senate floor.

New Provisions

The Senate bill allows NCUA to add groups of over 3,000 if the agency decides a group cannot sustain its own

credit union, or to accommodate a safety and soundness merger.

Additionally, the Senate Banking Committee bill would -

Increase audit requirements.

Federal credit unions over 5500 million would be required to obtain an independent CPA audit. Institutions between \$10 million and \$500 million must use an independent CPA if they chose to have an outside audit. Federal credit unions under \$10 million are exempt.

Ease conversion requirements.

An amendment recommended by Senator Shelby (R-Ala.), and supported by fellow Republican committee members, would ease current conversion requirements. The Senate bill stipulates that credit unions need approval from 50% of the voting members to convert to another type of financial institution rather than consent from 50% of the members, which NCUA currently requires.

The bill would tighten notification requirements. Credit unions that want to convert to a mutual savings bank would be required to notify members three times: 90- 60- and 30- days prior to the conversion vote.

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Curb member business lending.

Changes would limit member business loans to the lesser of 1.75% times net worth (retained earnings under GAAP) or 1.75 times 7% of assets, whichever is lower. NCUA has the authority to exempt credit unions chartered for, or with a history of primarily making member business loans. Loans under \$50,000 are exempt. Community development credit union business loans are also exempt.

Codify language.

The Senate bill would codify the long-standing credit union "once a member, always a member" policy. Bankers have filed a suit challenging this measure in California.

Add prompt corrective action when credit union capital falls below prescribed levels.

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News Briefs

- Deloitte & Touche issues clean audits - The National Credit Union Share Insurance Fund (NCUSIE7), Central Liquidity Facility, NCUA Operating Fund, and the Community Development Revolving Loan Program each earned unqualified opinions on 1997 financial statements audited by Deloitte & ToucheLLP.
- Grants available - Credit unions have until June 12 to apply for community development grants from the Treasury's Department's \$40 million Community Development Financial Institutions Fund.

Applications for technical assistance grants are due by May 29.

Interested credit unions should contact the Community Development Financial Institutions Fund, Department of the Treasury, 1500 Pennsylvania Avenue, NW, Washington, DC 20220, telephone (202) 622-8662 and fax (202) 622-7754.

NCUA News

NCUA News is published by the National Credit Union Administration, the federal agency which supervises and insures credit unions.

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Information about NCUA and its services may be secured by writing to the Office of Public and Congressional Affairs, or by calling 703-518-6300. News of what is happening at NCUA is available by calling 800-755-1030 or 703-518-6339.

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- NCUSIF Activity-At March 31, 1998, the NCUSIF equity level was 1.29 percent based on year-end 1997 insured shares of \$294.3 billion. No funds were add to the Reserve for Potential Losses account. Eight credit union failed through the first quarter.
- Capitalization deposit and operating fees-Credit unions were assessed \$235 million for NCUSIF capitalization deposit adjustments and operating fees during the first quarter of 1998.

ABOUT INVESTMENTS

How to Control Investment Risk

The NCUA Board adopted, April 16, 1998, the Federal Financial Institutions Examination Council (FFIEC) policy statement on Investment Securities and End-User Derivatives. Activities as NCUA Interpretative Ruling and Policy Statement (IRPS) 98-2.

The IRPS describes sound principles and practices for managing and controlling the risks associated with investment activities. It emphasizes that as a sound practice, credit unions should understand the characteristics of their investments, know the value and price sensitivity of their investments both prior to acquisition and periodically after purchase, and manage and control these risks. A credit union should not acquire a material position in an instrument until all responsible personnel understand and can manage the risks. Management reports that summarize activities and investment risk exposure should be submitted to the board for its review.

The IRPS will be used as an examination tool and it can aid your credit union as you seek more risk assessment guidance.



Senate Passes CU Bill

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The Senate version enhances the prompt corrective action section of H.R.1151 with more detailed language found in recommendations from the Treasury Department's recent study.

What's Next

It is doubtful that a vote will occur in the full Senate before the May 22 Memorial Day recess begins. After the Senate votes, two scenarios are possible. If the final Senate bill is significantly different from H.R. 1151, a conference committee of top-ranking House and Senate Banking Committee members would meet to construct a compromise bill. The House and Senate would then revote the final bill.

If the final Senate bill is similar to the House bill, a joint conference would be unnecessary and the Senate would send its bill to the House to re-pass before forwarding it to the President for signature.

Herb Yolles is Temporary Deputy Executive Director

Risk Management Director and Central Liquidity Facility President Herbert S. Yolles is currently serving a 90-day appointment as deputy executive director of NCUA.



Herb Yolles

During the past 20 years, Yolles has served as the agency Controller and Director of Financial Operations. A certified public accountant, he has an accounting degree from the University of Delaware, and an MBA from George Mason University, Fairfax, Va.

New Atlanta Phone Numbers

Effective May 11, the NCUA Region III Atlanta office telephone number changed to (678) 443-3000 and the Region III FAX number became (678) 443-3020.

BOARD ACTIONS

APRIL 16, 1998

NCUA Broker-Dealer, Safekeeping Provisions

The NCUA Board adopted final amendments to Part 703 that were issued last year as interim amendments. These final amendments revise the brokerdealer and safekeeping provisions of the investment rule. The Board also removed the High Risk Securities Test for CMO's and REMICs from Part 703 and 704 because the Board is adopting a new policy statement on managing investment risks. (See belong)

New Investment Policy

The Board approved the Federal Financial Institutions Examination Council's Supervisory Policy Statement on Investment Securities and End-User Derivatives Activities. Issued as Interpretive Ruling and Policy Statement 98-2, the document offers guidance on sound practices for managing the risks of investment activities. This new policy statement replaces IRPS 92-1 published February 3, 1992.

IRPS 98-2 is being distributed to federal credit unions and now appears on NCUA's web site at <http://www.ncua.gov/ref/IRPS/IRPS.html>. The investment article on page 2 offers more details.

Board Denies PFCU Appeal

The Board denied Pentagon Federal Credit Union's (PFCU) appeal of an overlapped field of membership (FOM) expansion. Pentagon is appealing a Department of Army decision to award Andrews AFB FCU a credit union franchise in Belgium. PFCU argued that the personnel stationed in Belgium falls within their FOM.

"Technically, the personnel in Belgium do fall within the PFCU's current FOM because of broad language regarding DOD-personnel outside the U.S.," said Deputy General Counsel Jim Engel. "However, the selection follows the For-

eign Geographic Franchise Assignments." Engels told the Board "PFCU's complaint is with the selection process used by the Army."

Year 2000 Update

NCUA's Director of Strategic Planning Layne Bumgardner updated the NCUA Board on Year 2000 (Y2K) initiatives.

New Vendor Authority

Using our new authority under Public Law 105-164, "NCUA plans to proceed with a Y2K-specific vendor examination program to identify readiness of the vendors' systems," Bumgardner reported to the Board. The scope of these examinations will identify:

- Status of the renovations to date.
- Specific target dates for release of corrected programs. Testing strategy and monitoring successful testing by credit union clients.
- Contingency planning.

Coming soon to NCUA's website: vendors' plans, target dates for testing, and target dates for release of compliant systems. Find additional details on page 5.

NCUA Internal Readiness

The Office of Technology and Information Services is conducting tests on NCUA's internal systems and hardware for Y2K compliance. A third party is reviewing this testing effort. NCUA is sending a letter to all credit unions to provide an update of NCUA's progress.

NCUA Approves Insurance and Charter Changes

Insurance Conversion

The NCUA Board approved the insurance conversion of \$102 million Aurora Earthmovers Credit Union, Aurora, Ill., from federal to private insurance on members' deposits. A majority of the credit union members voted to approve the insurance conversion February 4, 1998.

Charter Expansion

The NCUA Board approved the First Community FCU to expand its community charter to include all of the residents of Kalamazoo County, Mich. The expansion will provide FCU services to an additional 174,675 residents.

Charter Conversions

The NCUA Board approved the conversion of \$208.1 million AGE FCU, Albany, Ga, from occupational to community charter. AGE will serve Lee and Dougherty Counties plus the low-income communities of Mitchell and Worth Counties, Ga.

The NCUA Board also approved the conversion of \$9 million Walker County FCU, Huntsville, Texas, to a community charter able to serve low-income Walker County, Texas.

Disclosures Necessary for Federal EFT Payment

Many credit unions are establishing electronic fund transfer (EFT) accounts for members who receive regular federal payments to accommodate new law, "EFT 99," which stipulates that nearly all federal payments must be made electronically by January 1, 1999.

As credit unions arrange for EFTs, perhaps through a corporate credit union, please remember that such arrangements may give an uninsured third-party provider access to EFT deposits of members' insured accounts.

It is important to provide the appropriate disclosures to members. This includes the fees and costs imposed by all parties, the legal relationship involved, and an explanation of the applicability of federal deposit insurance insofar as it is relevant to this arrangement. Disclosures should be constructed carefully so members are not misled about EFT '99 requirements.



Y2K - Frequently Asked Questions

Year 2000 Questions and Answers - The following questions have been asked by credit unions, information system vendors (ISVs), and examiners.

1. What is a mission critical system? What happened to the three categories of systems listed in NCUA Letter to Credit Unions 97-CU12?

A mission critical system is one where failure would have catastrophic results for the credit union. For example, a credit union's share and loan data processing system may be a mission critical system. In this example the system includes all of the components needed to process share and loan data (i.e., computer hardware and software).

The three categories of systems (mission critical, essential, non-essential) still exist. NCUA's Year 2000 contingency plan makes many references and has specific requirements for mission critical systems. However, the quarterly report uses two broader categories (critical and non-critical). It is the credit union management's responsibility to categorize their systems into priority order that can be summarized into the broader categories.

Systems designated as "essential" pose the greatest classification challenge since these systems would ideally be updated before January 1, 2000; however, resources may not permit the upgrade. Management must make tough decisions classifying these systems as either critical or non-critical depending on available resources and member needs/expectations.

2. Our credit union has one computer system that meets all of our data processing needs - how do we report this system on the Year 2000 Quarterly Report? A vendor sold us the system and they provide us with updates and technical support - does this affect our reporting ?

The quarterly report instructions contain two sections that speak directly to this situation.

Briefly, the one system that does everything is called an integrated system and it can be reported as one system, or you may consider each major component as a separate system. Many small credit unions rely on integrated systems - a correct way to report these systems is to list one system under the share and loan section of the appropriate phase (renovation, testing, or implementation).

The answer to the second part of your question is, the vendor supported systems should be listed under the renovation phase until the vendor supplies a Year 2000 version for the credit union to test. The quarterly report instructions give the specifics for listing the system in the appropriate completion column. For example, if a vendor has not provided its Year 2000 release, and they state the system is in the testing phase (for the vendor, not the credit union), the credit union will report that system in the renovation phase in the 51 -75 percent completed column. Additional examples can be found in the instructions for the quarterly report.

3. If we receive certification from an outside vendor, do we still need to perform testing?

The answer to this question is found in NCUA Letter to Credit Unions 97-CU-12. The letter states that "credit unions should not take a vendor's, or third-party's certification that vendor assertions that a system is compliant...the system must be tested in the credit union's environment." NCUA is currently in the process of evaluating testing requirements. Upon completion of this evaluation, NCUA will issue a Letter to Federally Insured Credit Unions to provide additional guidance.

4. What documentation should be available for the examiners to review at our next exam?

To facilitate the Year 2000 review, the examiner will need the following items:

- Assessment and detailed inventory of systems and their components;
- Project plan and project team minutes; Contingency plan;
- Correspondence between the credit union and any third party regarding Year 2000 compliance (e.g., vendors, sponsors, manufacturers, third-party servicers);
- Agreements and any other correspondence between the credit union and any external parties engaged to assist in the Year 2000 project; and
- Testing documentation including: the plan, the results, and any follow-up.

5. What should our contingency plan include? Where does our responsibility end ?

The contingency plan should include an alternative path to ensure mission critical systems are ready for Year 2000. Some of the key elements are (1) trigger dates for execution, (2) estimated time to implement, (3) estimated cost to implement, and (4) operational items such as liquidity and staffing needs. For more

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Y2K Q&A

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detailed information, please refer to *NCUA Letter to Credit Unions 98-CU-2*.

To answer the second part of your question, your responsibility is to provide service to your membership. If member services disappear without notice on January 1, 2000, your members will be the final judge of your preparation. Your plan should include anything that you can control and should exclude items that are obviously beyond your control.

6. How do I get started on the testing phase?

The first step in the testing phase is to develop a test plan. The plan should include the following items:

- Identify critical transactions and processes;
- Establish testing criteria; Establish expected results;
- Develop test data;
- Review any input, display, or storage of dates;
- Establish estimated testing dates; and
- Determine testing completion dates.

NCUA plans to issue a letter in the near future to assist credit unions in performing the testing phase.

How NCUA Will Implement New Y2K Vendor Authority

Because Year 2000 readiness is imperative, NCUA will use the regulation and examination authority Congress recently provided over information systems vendors to assure the safety and soundness of credit unions.

NCUA plans to review vendors that offer electronic data processing services to credit unions to ascertain the following:

- Status of Y2K renovation to date.
- Schedule of release dates. -
- Testing strategy and oversight of successful testing by credit union clients.
- Contingency planning.

A "Summary of Findings" will be provided to credit unions and may be posted on NCUA's web site.

Vendor Conference Held

NCUA held a vendor conference in mid-May to jointly develop sound strategies that assist credit unions to complete the testing phase of Year 2000 compliance.

NCUA used the meeting as a forum to discuss the new law's impact on vendors, the agency's initial vendor examination and regulation plans, and to attain guidance for testing strategies of Y2K compliance. NCUA will develop and distribute a guidance paper on testing strategies subsequent to this meeting.

Web site Information

To keep credit unions informed of vendor Y2K readiness, NCUA plans to electronically publish key information about each applicable vendor. NCUA's Year 2000 web site will include:

- Name, phone, fax number and web site address for each information system vendor;
- Scheduled beta test release date for the continuing version available from each vendor; and
- Scheduled full release date for their Y2K compliant version.

As vendors submit updated information, the web site will also be updated.

ABOUT INVESTMENTS

Credit Union Policies

The Part 703 investment rule adopted last year emphasizes credit union investment policies and the responsibilities of a credit union's board of directors.

Each board should ensure the credit union stays within its "comfort zone" in making investments.

For example, if a board member is not comfortable with anything beyond short term Treasuries or simple certificates of deposit, the investment policy should be limited to these instruments. If they understand and are comfortable with more complex investments,

the investment policy could authorize their purchase.

To avoid any misunderstanding, detailed policies are important. For example, instead of a blanket authorization of floating rate notes, the policy could state: authorize floating rate securities linked to 3-month LIBOR, with a maturity not to exceed 5 years, as long as the cap is 300 basis points above the coupon at the time of purchase and the securities do not exceed [some percentage] of capital.

Investment policies do not require as much detail if they are expressed in risk terms. As an alternative, the policy could state: the total portfolio value should not decline by more than [a specific percent]

of capital for a rate increase of 300 basis points, and income should not change by more than [some amount].

If policy includes using risk limits, ensure a reliable way to measure risk exposure. The related investment committee, usually the asset-liability committee, should get detailed reports verifying the credit union is staying within its policy limits. The board should receive summary reports.

The board must ensure that the credit union's investment officers understand the investments they buy and be able to explain them to relevant credit union staff, to the board, and to the examiner. An investment should not be authorized if it is not understood. Adopting a "boilerplate" policy and affixing the credit union's name almost guarantees problems.



OPM Executive Named NCUA Director of Human Resources

Sherry D. Turpenoff became NCUA Director of Human Resources May 4 based on her 27-year history as an expert in human resource management and development.

Making the announcement, Chairman Norman E. D'Amours said, "After a lengthy review process, Sherry Turpenoff was selected from a group of excellent candidates based on her strong leadership skills, proficient technical knowledge, depth of integrity, strategic vision and communication skills. Ms. Turpenoff is a recognized leader in the human resources field, especially known for her innovative and creative skills, and we welcome her to NCUA."

Sherry Turpenoff holds a BA degree from Southern Illinois University, Edwardsville, III. A few of her numerous awards are the Vice President's Hammer Award for Reinvention, OPM Director's

Award, OPM Special Outstanding Award, and the US Department of Justice Superior Accomplishment Award.

Ms. Turpenoff joins NCUA after serving more than a quarter century in personnel positions with a university, the Army, and OPM. Most recently, she has been the OPM Director of Nationwide Examining Policy and Office of Administrative Law Judges. In this position, she headed the federal examination program and the recruitment, examining, and employment of administrative law judges for 30 federal agencies.

Her previous assignment was Staffing Operations Director responsible for changing the monolithic, regulation-based federal staffing system to a flexible agency-tailored system. She also served as the Chief of Financial, Administrative, Social Sciences, Examining Division at OPM.

Turpenoff's career began as a personnel officer at Southern Illinois University in 1971. She moved to the US Civil Service Commission as a personnel staffing specialist in 1973. As her career advanced, she held numerous human resource positions at OPM and with the US Army.



<http://www.ncua.gov>

Many publications including NCUA News are available to download directly from the NCUA web site.

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